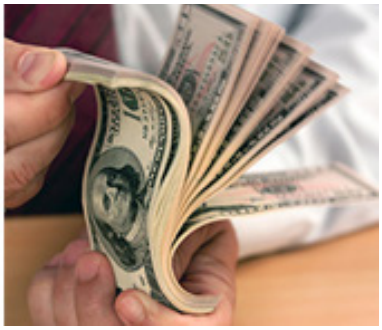
Indiana Manufacturers Association

IMA Tax Talk



Indiana's Leading Voice for Industry

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Selected Sales and Use Tax Rulings: September to December, 2012

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Indiana manufacturers experienced both wins and losses on sales and use tax protests before the Indiana Department of Revenue in the last four months of 2012.

Department exempts chemical cleaner used by plastic container manufacturer. The Department assessed sales tax against acetone that it claimed was applied "in between" production runs, i.e. in either pre- or post-production. Taxpayer uses "rubber blankets" in printing text and designs on the plastic containers it manufactures. Acetone is manually applied to clean the blankets. Citing 45 IAC 2.2-5-12(d), the department's auditor asserted that cleaning took place while production was stopped and was not an "automated continuous process." Rather, Taxpayer uses the acetone outside of the production process as part of its "routine maintenance activities." The auditor conceded that the acetone was needed for production to continue, but its use was "ultimately secondary to production of plastic containers." The Department explained that being "necessary" for production was not alone sufficient to justify exemption, see Ind. Code § 6-2.5-5-5.1(b) (exempting tangible personal property acquired to be directly consumed in direct production of other tangible personal property). The property must also be an "integral part of an integrated process." See 45 IAC 2.2-5-10(g). The Department found that "use of the acetone is sufficiently distinguished from the routine use of cleaning supplies commonly found and used during various manufacturing processes." The acetone was directly consumed in the direct production of Taxpayer's products and therefore exempt from sales tax. See Letter of Findings No. 04-20120337 (2006 – 2008 tax years) (posted 11/28/2012).

Modular home platforms transporting work-in-process partially exempt from use tax. Taxpayer designs, manufactures and sells modular homes. The Department assessed use tax against modular home platforms, which are large platforms with wheels. During construction, the homes are moved from station to station on the platforms. Taxpayer attaches modular home parts to the platforms. Pointing to 45 IAC 2.2-5-8(f)(3), the Department notes that transportation equipment used to transport work-in-process or semi-finished materials to or from storage is exempt if the transportation is within the production process. The platforms were exempt when used to transport the modular homes during production and taxable when used to transport the homes after production. The Department determined that the platforms transported homes post-production one day out of ten and applied a 90% exemption from use tax. See Letter of Findings No. 04-20120050 (2008 – 2010 tax years) (posted 9/26/12).

Concrete pumper was taxable as contractor, not an exempt manufacturer. Taxpayer pumps concrete for use in mining infrastructure, other construction, and preset molds. It supplies both the concrete and the pumping equipment to customers. The Department assessed use tax on the purchase of a pumping truck, line pump, and related repair and service parts. Taxpayer argued that because the truck and equipment were acquired for direct use in manufacturing, they were exempt under Ind. Code § 6-2.5-5-3(b). The manufacturing exemption applies to industrial processors who provide industrial processing or servicing and transfer the property back to the owner. See 45 IAC 2.2-5-10, Ind. Code § 6-2.5-4-2. And it applies to equipment used directly in extraction or mining. See 45 IAC 2.2-5-9. The Taxpayer, the Department concluded, was neither a mining operator nor an industrial processor. Its customers may be manufacturers or miners, "but Taxpayer is a contractor." Taxpayer owed use tax on the equipment and parts used to fulfill its contracts. See Letter of Findings No. 04-20110432 (2008 – 2010 tax years) (posted 9/26/2012).

Taxpayer's equipment used to produce "debris" from demolitions; it did not re-manufacture scrap metal. Seeking to recapture erroneously paid refunds, the Department assessed sales and use tax against an out-of-state Taxpayer who performs "asset retirement" (e.g. structural demolition, asbestos abatement and salvage segregation/disposal) throughout the United States. Taxpayer claimed that certain equipment, including a scrap handling magnet, generator, and hydraulic breaker, were used to "produce scrap." Taxpayer asserted that it is a scrap "re-manufacturer," not a "recycler." First, Taxpayer argued that the equipment was exempt under Ind. Code § 6-2.5-3-2(e) because it was delivered into Indiana by vendors for modification and shipment outside the state. The Department concluded that Taxpayer's documentation failed to support this argument.

Second, Taxpayer maintained that the equipment was ex-

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Selected Sales and Use Tax Continued

empt under Ind. Code § 6-2.5-5-3(b) because it was acquired for the direct use in the direct production of scrap metal. The Department noted that the General Assembly did not intend to create a "global" exemption for all equipment used within a manufacturing facility. To be exempt, the equipment must meet the "double direct" test and be "essential and integral" to the manufacturing of tangible personal property. Taxpayer outlined six steps of its "manufacturing process of ferrous material," starting with the identification of raw materials, continuing with the removal of contaminants, the reduction of materials to a manageable size, the sorting of materials, the processing of materials to customers' specifications, and concluding with storage of the materials for future shipment to customers. The Department observed that Taxpayer's actions produced "debris"; the scrap metal was a byproduct of its asset retirement services. And Taxpayer's demolition work did not constitute repair activities and could not be considered "re-manufacturing." The Department concluded: "One man's trash may be another man's treasure. However, simply separating/removing the unwanted parts, and sorting, cutting, and baling the salvaged parts (scrap metals) to be sold to the steel mills does not make Taxpayer a re-manufacturer of the 'scrap metals.'" Because Taxpayer was not engaged in "re-manufacturing," the Department did not decide if the equipment met the "double direct" test. The Department also concluded that replacement parts for equipment used in providing asset retirement services were not exempt. Letter of Findings No. 04-20120472 (posted 12/26/2012).

Die oven's use taxable as "one step removed" from production process. Taxpayer produces aluminum extrusions by heating billets to extreme temperatures and forcing the billets through dies in presses to produce the desired shapes. The dies must first be heated to several hundred degrees Fahrenheit in a die oven, which is located near the manufacturing presses. Cranes lift the dies onto Taxpayer's presses. Taxpayer asserted that the die oven was directly used in the direct manufacturing of the extrusions and therefore exempt under Ind. Code § 6-2.5-5-3(b). To be exempt, the Department's regulation provides that materials must have an "immediate effect on the article being produced." See 45 IAC 2.2-5-8(c). Property has an "immediate effect" if it is an "essential and integral part of an integrated process which produces tangible personal property." The Department agreed that the die oven was necessary and crucial to the manufacturing process. But the die oven did not have an immediate effect on the aluminum billets – the items used to produce the extrusions. The Department found that the die oven's use is "one step removed from the actual manufacturing process. Thus, it was subject to use tax. See Letter of Findings No. 04-20120362 (2008 – 2010 tax years) (posted 11/28/12).

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